Office-Supreme Court, U.S.
FILED
SEP 10 1981
ALEXANDER L. STEVAS,
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No. 80-702

In the Supreme Court of the United States

OCTOBER TERM, 1980

UNITED STATES OF AMERICA, PETITIONER

v.

STATE OF NEW MEXICO, ET AL.

ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE TENTH CIRCUIT

BRIEF FOR THE UNITED STATES

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QUESTION PRESENTED

Whether contractors of the United States Department of Energy, engaged to manage and operate government-owned atomic research laboratories, are procurement agents of the United States, so that payments made by the contractors with the federal government's funds, to procure goods and to pay for the operational costs of the laboratories, are constitutionally immune from the New Mexico gross receipts and compensating use taxes.*

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* In addition to the State of New Mexico, the other respondents in this case are the Bureau of Revenue of the State of New Mexico, and Fred L. O'Cheskey, as Commissioner of Revenue of and for the State of New Mexico.

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OPINIONS BELOW

The opinion of the district court (Pet. App. 1a-10a) is reported at 455 F. Supp. 993. The opinion of the court of appeals (Pet. App. 11a-28a) is reported at 624 F.2d 111.

JURISDICTION

The judgment of the court of appeals (Pet. App. 29a-30a) was entered on June 2, 1980. By orders of August 15 and September 19, 1980, Mr. Justice White extended the time within which a petition for

a writ of certiorari could be filed to and including October 30, 1980. The petition for a writ of certiorari was filed on October 30, 1980, and granted on February 23, 1981. The jurisdiction of this Court rests on 28 U.S.C. 1254(1).

STATUTE INVOLVED

The pertinent parts of New Mexico's Gross Receipts and Compensating Tax Act, N.M. Stat. Ann. 1953, §§ 72-16A-3, 72-16A-4, 72-16A-7, 72-16A-12, 72-16A-12.1, 72-16A-12.2, 72-16A-14, and 72-16A-14.9 (Supp. 1975), are set forth in the App., *infra*, 1a-4a.

STATEMENT

1. Sandia Corporation was organized in 1949 as a special subsidiary of Western Electric Company, Inc., for the purposes of performing research and development for the United States Atomic Energy Commission (now the Department of Energy (DOE)) in New Mexico (Pet. App. 14a). It is not involved in any private work, receives no fee or profit under its contract, and owns no property except the $1,000 in United States bonds that constitutes its paid-in capital (Pet. App. 3a).

The Zia Company is a subsidiary of Santa Fe Industries, Inc. Since 1946, Zia has performed a variety of management, operational, maintenance, architect-engineer, procurement, and related functions in connection with DOE's Los Alamos Scientific Laboratory (Pet. App. 14a). Zia performs separate private work with a distinct set of records, employees and locations. Virtually none of Zia's private prop-

erty is involved in performance of its contract with DOE (Pet. App. 3a, 14a).

Los Alamos Constructors, Inc. (LACI) is a subsidiary of the Zia Company. It is devoted exclusively to the performance of construction work in support of the Los Alamos Scientific Laboratory, a government-owned research and development facility (J.A. 22-29).[1] LACI owns no tangible personal property and makes no purchases. Rather, it procures the property it needs for performance of its Los Alamos contract through Zia. All of LACI's activities are managed by its parent Zia. Zia and LACI are paid fixed fees annually for work performed under their contracts with DOE (Pet. App. 3a-4a, 14a).

The management contracts between DOE and Sandia, Zia, and LACI are standard Atomic Energy Commission (now DOE) management contracts. This type of contract was developed to facilitate the Atomic Energy Commission's substantial reliance upon private industry in the construction and management of large research and development facilities (Pet. App. 13a).[2] The standard DOE atomic facility management contract provides that title to all tangible personal property passes directly to the government from the vendor. Thus, the contractors do not own any of the tangible personal property they procure. Moreover, the contract also places the risk of loss upon the government for property procured under the contracts. Finally, the contract provides for government control over the disposition of the property and government approval of property management procedures employed by each contractor (Pet. App. 4a).

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[1] "J.A." refers to the Record Appendix.

[2] See generally Hiestand and Florsheim, *The AEC Management Contract Concept*, 29 Fed. Bar J. 67 (1969).

The tangible personal property procured by Sandia and Zia and all other operational costs incurred under the contracts, such as salaries, are paid for under an "advanced funding" procedure. Under this procedure, the contractors pay vendors and employees with drafts drawn directly on United States Treasury funds maintained in a depository bank account, under the authority of a letter of credit to cover withdrawals (Pet. App. 4a) (J.A. 19, 26).

The "advanced funding" procedure employs a special bank account established by the contractor, the United States, and a designated bank, pursuant to a three-party contract (J.A. 84-85b, 86-88, 89-90a, 92, 95, 96, 109-113). The United States owns any balance in the account (J.A. 19-20), but the contractor has the right to execute drafts payable to third parties in order to pay any expenses incurred in performing the underlying government contract. DOE thereupon issues a letter of credit to an appropriate Federal Reserve Bank in favor of the contractor. The letter of credit provides the general authority for the Federal Reserve Bank to make United States Treasury funds available for deposit in the special bank account (J.A. 95, 96). When a contractor incurs an expense under the contract, it pays the expense by executing a draft payable to the creditor and drawn on the special bank account. At the same time, the contractor or the bank executes a payment voucher in an amount sufficient to cover the draft and the Federal Reserve Bank, on the basis of the voucher, transfers funds into the special bank account (J.A. 109-113) (Pet. App. 22a n.8).

Under the contract, the government owns the funds in the special accounts and controls the disposition of such funds (J.A. 19, 26, 32-33). The liability

provisions of the contract require the government to pay all operational costs and further stipulate that no contractor funds are to be used to pay for contract costs. Obligations that are "properly incurred" by the contractors are therefore treated as DOE liabilities. Hence, if the government failed to provide funding, the contractors would be excused from performance of the contracts and the government would be liable for all properly incurred and reported claims (Pet. App. 4a-5a).

Prior to July 1, 1977, DOE's contracts with Sandia, Zia, and LACI did not refer to the contractors as "agents" of the government. On that date (which was during the pendency of this litigation), the contracts were modified to specify that the contractors are "agents for and on behalf of ERDA for certain purposes" (Pet. App. 26a), in recognition of the "long standing agency status and authority" of the contractors (Pet. App. 6a; J.A. 49-61). The amendments also stated that they "shall not be construed to modify any other provisions of the contract * * * nor shall [they] create rights or obligations not otherwise provided for in the contract" (Pet. App. 26a).

2. The New Mexico gross receipts tax is levied upon the gross receipts realized by persons engaged in the construction business or in performing services of a professional, technical, or scientific nature. There is also a compensating use tax equivalent to the gross receipts (sales) tax that is imposed upon the use of tangible personal property that has been imported into and used within the State without the payment of any gross receipts (sales) taxes. See App., *infra*, 1a-4a.

Prior to 1967, the New Mexico Bureau of Revenue acknowledged that the contractors engaged under the standard Atomic Energy Commission contracts were agents of the United States. The State therefore did not impose any taxes on the type of transactions involved in this case. In 1967, however, the State changed its position with respect to the relationship between the contractors and the government and sought to impose such taxes on the ground that the contractors were not agents of the United States (Pet. App. 6a). The State of New Mexico thereupon assessed gross receipts and compensating use taxes against Zia and LACI for the period January 1, 1966, through June 30, 1967, with respect to their disbursement of government funds and their out-of-state procurement of tangible personal property. After the State Commissioner of Revenue upheld the assessments, the United States and the contractors appealed to the Court of Appeals of New Mexico.[3] The New Mexico Court of Appeals reversed the Commissioner of Revenue's determination imposing gross receipts and compensating use taxes on the contractors' disbursement of federal funds and purchasing of tangible property. See *United States* v. *Bureau of Revenue*, 87 N.M. 164, 531 P.2d 212 (1975). It held that the Commissioner was estopped to assess the taxes in question because of his previous rulings that the contractors were agents of the United States and therefore immune from state taxation on their expenditures made with the federal government's funds. A concurring judge concluded that even on the as-

[3] The government and the contractors conceded liability for the gross receipts tax on the annual fixed fees paid as compensation for the contractors' services. Accordingly, those fees are not at issue in this case.

sumption that estoppel was unavailable, the New Mexico taxes could not be imposed upon the contractors' disbursements and purchases (see 87 N.M. at 166-170; 531 P.2d at 215-218).

Following the decision of the New Mexico Court of Appeals, the DOE requested the New Mexico Commissioner of Revenue, by letter dated January 30, 1975, to concede that contractors such as Zia and LACI were not liable for the gross receipts and compensating use taxes on their disbursements and procurements, and to authorize the contractors to issue permanent nontaxable transaction certificates in purchasing tangible personal property (J.A. 13-15). On February 28, 1975, the New Mexico Commissioner advised DOE that he refused to do so "until the courts finally address the important questions involved." In the State Commissioner's view, the New Mexico Court of Appeals' estoppel ruling had not resolved the substantive tax immunity issue and therefore another test case was necessary (J.A. 16-17).

3. Accordingly, on July 17, 1975, the government brought this action against the State of New Mexico in the United States District Court for the District of New Mexico for a declaratory judgment that sales of tangible personal property to DOE, through its management contractors Sandia and Zia, are sales to the United States that are exempt from the New Mexico gross receipts and compensating taxes, and that the advanced funds disbursed under the management contracts here are not subject to such taxes (Pet. App. 1a-2a, 11a-12a; J.A. 6-12).

The district court concluded "that Sandia and Zia are procurement agents of the United States and that any sales of tangible personal property to them are sales to the United States through its procure-

ment agents, which are not subject to the 4% gross receipts tax imposed by the New Mexico Gross Receipts and Compensating Tax Act" (Pet. App. 7a). It also held that the contractors are not subject to the compensating tax for their purchases of tangible personal property in other states (*ibid.*).

The district court further held that the advanced funds disbursed by Sandia, Zia and LACI are not compensation for services subject to the New Mexico gross receipts tax, but are funds that belonged to the government and were disbursed by the contractors to pay operational costs. In support of this conclusion, the district court observed that Zia and LACI received a fixed fee as compensation for their services, upon which they paid gross receipts taxes, and that Sandia received no fixed fee or profit. Moreover, the court pointed out that under the advanced funds procedure, the funds deposited by DOE in the special bank accounts were the only monies available for payment of all the contractors' operational costs. Those funds were not to be disbursed in any manner inconsistent with contract performance. DOE could exert direct control over the disbursement of the funds and retained title to the funds while they were on deposit with the bank (Pet. App. 8a-9a). Accordingly, the district court upheld the government contractors' immunity from New Mexico gross receipts and compensating use taxes and entered a declaratory judgment in favor of the government (Pet. App. 10a).

Finally, the district court rejected the State's argument that DOE had no authority to modify the contracts in 1977 to characterize Sandia, Zia and LACI as "agents." The court regarded the amendments to the contracts as simply confirming the na-

ture of the relationship that had always existed under the contracts. As the district court stated, "the Government and the contractors herein maintained an agency relationship for procurement purposes during the years of operation prior to the contract modifications, and have continued to do so to the present. They were not taxable before the modifications, because such modifications merely made the relationship more express, but did not change the agency relationship which had been in operation for three decades, and which had been recognized as such by the Bureau [of Revenue]" (Pet. App. 6a).

4. The court of appeals reversed (Pet. App. 11a-26a).[4] It held that Sandia, Zia, and LACI were not agents of the United States and were therefore subject to New Mexico gross receipts and compensating use taxes. After reviewing this Court's decisions dealing with the state tax immunity of government contractors, the court of appeals acknowledged that "[a]lthough there is language in these Supreme Court opinions suggesting that the results turn on traditional agency principles * * * it seems evident that the Court is more concerned with preserving the delicate financial balance between our co-existing

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[4] In the district court, the State argued that the United States had no right to challenge the imposition of the taxes at issue because it was not the "taxpayer" (Pet. App. 2a). The district court held that because the contracts require the United States to pay all costs under the contracts including taxes, the federal government as the real party in interest was the appropriate party to challenge the taxes on the ground of its constitutional immunity (Pet. App. 9a-10a). See *United States* v. *Bureau of Revenue*, 291 F.2d 677 (10th Cir. 1961); *Marquardt Corp.* v. *Weber County*, 360 F.2d 168 (10th Cir. 1966). The court of appeals affirmed this aspect of the district court's ruling (Pet. App. 26a-27a).

sovereignties than with rigid adherence to agency law terminology" (Pet. App. 17a). The court of appeals further observed that "[t]he trend toward restricting tax immunities * * * reflects an awareness of the serious threat posed to state revenues by ballooning governmental dealings in the private sector" (*ibid.*).

In holding that the contractors were not agents, the court of appeals sought to distinguish two decisions of this Court, *Kern-Limerick, Inc.* v. *Scurlock*, 347 U.S. 110 (1954), and *Livingston* v. *United States*, 364 U.S. 281 (1960) (per curiam), aff'g 179 F. Supp. 9 (E.D. S.C. 1959) (three-judge court), both of which upheld the immunity of contractors from state sales taxes in comparable circumstances on the ground that they were agents of the government.

As the court of appeals viewed the matter, the language in the request for bids, the contract, and the purchase order in *Kern-Limerick* more "clearly and uniformly disclosed an intention for the government to be directly obligated to the vendor for the contractor's purchases" than did the documents here (Pet. App. 15a). Although the court attempted to distinguish *Livingston* on the ground that the contractor in that case earned no fee (*id.* at 16a), it acknowledged that in the present case Sandia likewise earned no fee. However, the court of appeals "decline[d] to hang agency status, and thereby the welfare of state treasuries, on the existence or amount of a fee" (*id.* at 25a).

Finally, the court below rejected the government's argument that the advanced funding procedure conclusively established that Sandia, Zia and LACI were procurement agents that pledged the credit of the

United States vis-a-vis the third-party vendors. In the court's view, "[a]dvanced funding is simply another means of reimbursement devised by accountants to eliminate major weaknesses in the government's bookkeeping practices" (*id.* at 23a). Accordingly, the court of appeals was unwilling to attribute any significance to the 1977 contract modifications that explicitly confirmed that Sandia, Zia, and LACI are "agents for and on behalf of ERDA for certain purposes" (Pet. App. 26a). As the court stated, "[b]ecause we are convinced that, as a matter of law, the provisions of the contracts before the amendments did not establish agency status, we need not be swayed by amendments which make no changes" (*ibid.*).

SUMMARY OF ARGUMENT

1. In *M'Culloch* v. *Maryland*, 17 U.S. (4 Wheat.) 316 (1819), this Court first announced the doctrine that the federal government is immune from state taxation. "[U]nshaken, rarely questioned * * * is the principle that possessions, institutions, and activities of the Federal Government itself in the absence of express congressional consent are not subject to any form of state taxation." *United States* v. *County of Allegheny*, 322 U.S. 174, 177 (1944). See also *Department of Employment* v. *United States*, 385 U.S. 355 (1966); *United States* v. *Tax Commission of Mississippi*, 421 U.S. 599, 612-613 (1975). Federal tax immunity is "the unavoidable consequence of that supremacy which the constitution has declared." *M'Culloch* v. *Maryland*, *supra*, 17 U.S. (4 Wheat.) at 436.

In determining the reaches of the federal government's constitutional immunity from state taxation,

this Court has often extended the doctrine to protect private contractors who act on behalf of the United States. Thus, prior to *James* v. *Dravo Contracting Co.*, 302 U.S. 134 (1937), and *Alabama* v. *King & Boozer*, 314 U.S. 1 (1941), it had been held that a private contractor could not be subject to state taxation in connection with his performance of a government contract if he could pass the cost of the tax on to the federal government. However, in *King & Boozer* the Court abandoned this "economic burden" test and ruled that federal sovereignty "does not spell immunity from paying the added costs, attributable to the taxation of those who furnish supplies to the Government and who have been granted no tax immunity" (314 U.S. at 9). There, however, the legal incidence of the tax was on the private vendors, and the contracts provided that the contractor was to purchase the materials in its own name and on its own credit. The government was not bound by the contractors' purchase contracts but would reimburse the contractor only after the goods were delivered and inspected. In those circumstances, the Court concluded that the government's prerogatives under the contracts did not confer upon the contractor the status of an agent empowered to pledge the credit of the United States (see *id.* at 13).

Kern-Limerick, Inc. v. *Scurlock*, 347 U.S. 110 (1954), employed the Court's earlier analysis in *King & Boozer* in holding that sales to a federal contractor was entitled to immunity from state sales tax if the contractor was an agent of the federal government empowered to pledge the credit of the United States. There, the Court held unconstitutional the Arkansas sales tax as applied to purchases by a government contractor under a cost-plus-fixed fee contract, where the pertinent documents made it clear

that the contractor was acting as a purchasing agent for the government, title to the goods purchased passed directly from the vendor to the government, and the government was directly liable for payment of the purchase price. Accordingly, the Court concluded that "the Government is the disclosed purchaser and that no liability of the purchasing agent to the seller arises from the transaction" (347 U.S. at 121; footnote omitted).

2. The decision below rejecting the claimed immunity of the contractors in this case is contrary to *Kern-Limerick*, which we submit controls this case. Here, as in *Kern-Limerick*, the DOE management contracts to which Sandia, Zia and LACI are parties provide that title to all tangible personal property passes directly to the government from the vendors, and place the risk of loss directly on the government for property acquired under the contracts. The contracts further provide for government control over the disposition of the property and approval of property management procedures employed by each contractor.

Finally, and most importantly, the advanced funding arrangement, under which the contractors do not expend any of their own funds for goods or services but are able to disburse monies that at all times belong to the government, "gave to the contractors the status of agents of the Government to enter into contracts or to pledge its credit." *Alabama* v. *King & Boozer*, *supra*, 314 U.S. at 13. As the Fourth Circuit correctly observed in *United States* v. *Forst*, 569 F.2d 811 (1978), "the key factor in the case was whether the credit of the United States or the contractor was bound by the purchasing agreements" (*id.* at 811). Since Sandia, Zia, and LACI were empowered to write checks on government-owned funds, their power to bind the United

States and pledge its credit cannot seriously be questioned.

Contrary to the court of appeals' conclusion, the advanced funding procedure cannot be dismissed as "simply another means of reimbursement devised by accountants * * *" (Pet. App. 23a). There is a considerable difference between the case where the contractor expends its own funds and must await reimbursement by the government and the case in which the contractor is empowered to draw directly on the funds of the government. While the former case may not be inconsistent with an agency relationship (as *Kern-Limerick* itself demonstrates), it is at least clear that in such a case the contractor must rely upon the government's ratification of its actions in order to obtain reimbursement for its outlays. Here, the contractors did not take even that risk, for they disbursed *government* funds to the vendors and to their employees in the first instance. In every sense of the word, the contractors here acted on behalf of the government vis-a-vis the vendors. If sales to a contractor receiving after-the-fact reimbursement in *Kern-Limerick* were deemed to be sales to an agent of the United States, and thereby immune from state taxes, there is a stronger case for immunity here because the contractors had the additional authority to disburse government-owned funds and pledge the credit of the United States.

Although the court of appeals acknowledged that the advanced funding procedure created "appearances" of agency status for the contractors (Pet. App. 22a), it resisted the conclusion that the contractors were immune from state taxes, relying on the fact that "[a]t most, the contractor may pledge to the limits of its letter of credit" (*id.* at 22a-23a).

As the court reasoned, "[s]een in this light, Sandia, Zia and LACI are like numerous businesses which deal under letters of credit from banks and other sureties" (*id.* at 23a).

But the conclusion that the contractors' purchases and disbursements were subject to state gross receipts taxes does not follow from the fact that their letters of credit were limited in amount. The claim of immunity here is only coextensive with the contractors' authority to act on behalf of the government. The fact that their authority, like the authority of many agents, was limited in dollar amounts does not refute the argument that they acted as agents of the government within the scope of their authority. Indeed, in *Livingston* v. *United States*, 364 U.S. 281 (1960), aff'g 179 F. Supp. 9 (E.D. S.C. 1959), this Court summarily affirmed a three-judge district court's decision that a South Carolina sales tax could not be imposed upon a contractor's purchases under a similar DOE standard management contract. The court of appeals sought to distinguish that case on the ground that it turned on the fact that the contractor earned no fee from the contract (Pet. App. 16a), in much the same fashion as this Court distinguished *Livingston* in *United States* v. *Boyd*, 378 U.S. 39, 45 n.6 (1964). However, the court of appeals also expressed doubt that "such a factual determination would today withstand appellate review" (Pet. App. 24a; footnote omitted) and therefore "decline[d] to hang agency status, and thereby the welfare of state treasuries, on the existence or amount of a fee" (*id.* at 25a).

But whatever the merits of such a distinction, the undisputed fact is that Sandia received no fee or profit under its contract with DOE (Pet. App. 3a).

At all events, the Court's distinction of *Livingston* in *Boyd* rests upon the assumption that the South Carolina tax in the former case was a "privilege"-type use tax comparable to the Tennessee use tax at issue in *Boyd*. Since it is undisputed that the New Mexico use tax is, by contrast, a compensating use tax designed to tax out-of-state purchases of property brought into the state, the fact that two of the contractors here earned a fee has no relevance.

3. Nor does the fact "that the agency terminology does not appear uniformly in all the documents relating to the contracts" (Pet. App. 26a) effectively distinguish this case from *Kern-Limerick*, as the court of appeals apparently believed. Much the same argument was advanced by the State of Tennessee and rejected by the Tennessee Supreme Court in *United States* v. *Boyd*, 211 Tenn. 139, 363 S.W.2d 193 (1962), aff'd on another issue, 378 U.S. 39 (1964). There, the Tennessee court held that the contractor under the identical standard DOE management contract with advanced funding was immune from state sales taxes. In response to the argument that the contract did not in all respects employ the identical *Kern-Limerick* terminology of "agency," the court stated, in terms that are equally appropriate here (211 Tenn. at 155; 363 S.W.2d at 200): "The mere placing of terms such as agent or independent contractor in the contract does not make them such in law. The surrounding facts and circumstances determine the relationship."

Finally, the court of appeals stated that it was "highly skeptical of the sporadic addition of 'magic words' to a contract in an attempt to avoid state taxation" (Pet. App. 26a). But the modifications to the contracts were simply designed to confirm the status of the contractors as procurement agents of the

United States. Indeed, this Court in *Kern-Limerick* specified that "the form of contracts, when governmental immunity is not waived by Congress, may determine the effect of state taxation on federal agencies, for decisions consistently prohibit taxes levied on the property or purchases of the Government itself" (347 U.S. at 122-123; footnotes omitted). The form of these standard DOE atomic management contracts establish the immunity of the contractors from New Mexico sales and use taxes.

ARGUMENT

THE CONTRACTORS HERE ARE PROCUREMENT AGENTS OF THE UNITED STATES AND HENCE PAYMENTS MADE BY THEM WITH THE FEDERAL GOVERNMENT'S FUNDS TO PROCURE GOODS AND TO PAY FOR THE OPERATIONAL COSTS UNDER THEIR CONTRACTS ARE CONSTITUTIONALLY IMMUNE FROM THE NEW MEXICO GROSS RECEIPTS AND COMPENSATING USE TAXES

A. The Supremacy Clause of the Constitution Immunizes the Federal Government and its Agents from State Taxation

At issue in this case is whether the federal government's constitutional immunity from state taxation protects a private contractor's disbursement of the federal government's funds—in connection with its performance of a standard Department of Energy contract for the management of a government-owned atomic facility—from state gross receipts and use taxes. We submit that under the standard DOE contract for the management of atomic research laboratories at issue here, such contractors are procurement agents of the United States and that their disburse-

ments of advanced funds and purchases of goods under the contract are therefore immune from state gross receipts and compensating use taxes in the same manner as if the purchases had been made directly by the federal government itself.

Article VI of the Constitution provides that "[t]his Constitution, and the Laws of the United States which shall be made in Pursuance thereof; * * * shall be the supreme Law of the Land; and the Judges in every State shall be bound thereby, any Thing in the Constitution or Laws of any State to the Contrary notwithstanding." In *M'Culloch* v. *Maryland*, 17 U.S. (4 Wheat.) 316 (1819), this Court first announced the doctrine that properties, functions, and instrumentalities of the federal government are immune from state taxation. "[U]nshaken, rarely questioned * * * is the principle that possessions, institutions, and activities of the Federal Government itself in the absence of express congressional consent are not subject to any form of state taxation." *United States* v. *County of Allegheny*, 322 U.S. 174, 177 (1944). See also *Department of Employment* v. *United States*, 385 U.S. 355, 358-359 (1966); *United States* v. *Tax Commission of Mississippi*, 421 U.S. 599, 612-613 (1975); *United States* v. *County of Fresno*, 429 U.S. 452, 459 (1977). Federal tax immunity is "the unavoidable consequence of that supremacy which the constitution has declared." *M'Culloch* v. *Maryland*, *supra*, 17 U.S. (4 Wheat.) at 436.

In establishing the scope of the federal government's immunity from state taxation, this Court has often accorded constitutional protection from such taxes to private contractors who act on behalf of the United States. At the outset, the immunity was broad and virtually absolute in every instance where the federal government was made to bear the addi-

tional cost of the state tax. Thus, prior to *James* v. *Dravo Contracting Co.*, 302 U.S. 134 (1937), and *Alabama* v. *King & Boozer*, 314 U.S. 1 (1941), the Court had held that a private contractor could not be subject to state taxation in connection with his performance of a government contract if he could pass the cost on to the federal government. See, *e.g.*, *Panhandle Oil Co.* v. *Knox*, 277 U.S. 218 (1928); *Graves* v. *Texas Co.*, 298 U.S. 393 (1936).

However, in *Dravo* and in *King & Boozer*, the Court abandoned this "economic burden" test and ruled that federal sovereignty "does not spell immunity from paying the added costs, attributable to the taxation of those who furnish supplies to the Government and who have been granted no tax immunity" (314 U.S. at 9). There, the legal incidence of the tax was on the contractors, and the contracts provided that the contractor was to purchase the materials in its own name and on its own credit. The government was not bound by the contractors' purchase contracts but would reimburse the contractor only after the goods were delivered and inspected. In those circumstances, the Court concluded that the government's prerogatives under the contracts did not confer upon the contractor the status of an agent empowered to pledge the credit of the United States (see *id.* at 13). As the Court observed in the companion case of *Curry* v. *United States*, 314 U.S. 14, 18 (1941), "the Constitution, without implementation by congressional legislation, does not prohibit a tax upon Government contractors because its burden is passed on economically by the terms of the contract or otherwise as a part of the construction cost to the Government."

Thirteen years later in *Kern-Limerick, Inc.* v. *Scurlock*, 347 U.S. 110 (1954), the Court employed the *King & Boozer* analysis in ruling that sales to a federal contractor were entitled to immunity from

state sales tax if the contractor was an agent of the federal government empowered to pledge the credit of the United States. There, the Court struck down as unconstitutional the Arkansas sales tax as applied to purchases by a government contractor under a cost-plus-fixed fee contract, where the pertinent documents made it clear that the contractor was acting as a purchasing agent for the government, that title to the goods passed directly from the vendor to the government, and that the government was directly liable for payment of the purchase price. The Court concluded that "the Government is the disclosed purchaser and that no liability of the purchasing agent to the seller arises from the transaction" (347 U.S. at 121; footnote omitted).

In our view, the agency principle established in *Kern-Limerick* controls this case. As we shall show (pages 28-40, *infra*), here, as in *Kern-Limerick*, the DOE management contracts to which Sandia, Zia and LACI are parties, provide that title to all tangible personal property passes directly to the government from the vendors, and place the risk of loss directly on the government for property acquired under the contracts. The contracts further provide for government control over the disposition of the property and approval of property management procedures employed by each contractor. Finally, the advanced funding arrangement, under which the contractors do not expend any of their own funds for goods or services but are able to disburse monies that at all times belonged to the government, "gave to the contractors the status of agents of the Government to enter into contracts or to pledge its credit." *Alabama* v. *King & Boozer*, *supra*, 314 U.S. at 13. That is the fundamental prerequisite for a government contractor's claim of federal tax immunity.

B. The Contracts Here Designate the Contractors as Procurement Agents of the United States Empowered to Disburse Funds Belonging to the Federal Government

1. As we have pointed out (pages 19-20, *supra*), in *Kern-Limerick, Inc.* v. *Scurlock, supra*, 347 U.S. at 122, the contractor *Kern-Limerick* had a cost-plus fixed fee contract with the Department of the Navy which provided that all purchases made under the contract were made by the Navy, with Kern-Limerick acting only as its agent. The State of Arkansas sought to impose its sales tax on the contractor's purchases. The Court held that the question of who was the purchaser for state tax purposes was a federal question, that the legal incidence of the tax was on the purchaser, that the Department of the Navy was the real purchaser, and that the tax was therefore invalid. As the Court there stated, "[w]e find that the purchaser under this contract was the United States" (*ibid.*).

In so ruling, the Court distinguished its prior decision in *Alabama* v. *King & Boozer, supra*, 314 U.S. at 11, where the contractual provisions "plainly contemplate that the contractors were to purchase in their own names and on their own credit all the materials required * * *; that the Government was not to be bound by their purchase contracts, but was obligated only to reimburse the contractors when the materials purchased should be delivered, inspected and accepted at the site." For a private contractor to be cloaked with the government's immunity from state taxation, it must be clear under the contract that it is an agent empowered to bind the government or to pledge its credit. Thus, in *Kern-Limerick*, the Court cited as "[t]he significant difference" (347 U.S. at 119) between that case and *King & Boozer*

that both Kern-Limerick's request for bids and its purchase order contained the following provision (*id.* at 119-120):

> 3. This purchase is made by the Government. The Government shall be obligated to the Vendor for the purchase price, but the Contractor shall handle all payments hereunder on behalf of the Government. The vendor agrees to make demand or claim for payment of the purchase price from the Government by submitting an invoice to the Contractor. Title to all materials and supplies purchased hereunder shall vest in the Government directly from the Vendor. The Contractor shall not acquire title to any thereof.

Moreover, the arrangement between Kern-Limerick and the government required specific government approval to the purchasing agent for each request for bid and each purchase. Accordingly, the Court concluded "that the Government [was] the disclosed purchaser and that no liability of the purchasing agent to the seller [arose] from the transaction" (*id.* at 121; footnote omitted).

2. In ruling that the contractors here are not immune from state gross receipts and use taxes, the court of appeals suggested (Pet. App. 15a-17a) that subsequent decisions of this Court have undermined the authority of *Kern-Limerick*. But that case continues to stand as the leading precedent in determining the circumstances under which a private contractor serves as an agent of the United States so that its purchasing activities on behalf of the government are immune from state sales taxes. Indeed, the Court followed *Kern-Limerick* in *Livingston* v. *United States*, 364 U.S. 281 (1960) (per curiam), aff'g 179 F. Supp. 9 (E.D. S.C. 1959), with which the decision below

cannot be squared. There, this Court summarily affirmed a three-judge district court's decision that a South Carolina sales tax could not be imposed upon a contractor's purchases under a management contract between the Atomic Energy Commission and duPont that is virtually identical to the contracts at issue here. As the district court there stated, in terms that are equally applicable here, "[d]uPont's credit was not to be advanced or risked. Its disclosures in its requests for quotation and its purchase orders that the goods were being procured for the United States, to whom title would directly pass, and its imposition of the terms required of public contracts with the United States negatived any individual liability of its own. What obligations did arise from the purchase orders were discharged by drawing directly upon public funds" (179 F. Supp. at 21; footnote omitted).

The court of appeals sought to distinguish *Livingston* on the ground that it turned on the fact that the contractor earned no fee from the contract (Pet. App. 16a), in much the same way as this Court distinguished *Livingston* in *United States* v. *Boyd*, 378 U.S. 39, 45 n.6 (1964). But whatever the merits of such a distinction, the undisputed fact is that Sandia likewise received no profit or fee under its contract (Pet. App. 3a). At all events, the court of appeals also expressed doubt that "such a factual determination would today withstand appellate review (*id.* at 24a; footnote omitted) and therefore "decline[d] to hang agency status, and thereby the welfare of state treasuries, on the existence or amount of a fee" (*id.* at 25a).

In our view, this Court's reference in *Boyd* to the fact that the contractor in *Livingston* earned no fee is best explained in the context of the question presented to this Court in *Boyd*, *i.e.*, the validity of a

Tennessee use tax on the privilege of using tangible personal property for profit and gain irrespective of the title of the property or its importation (see 378 U.S. at 40-41 n.3, 43).[5] Accordingly, the fact that the contractor in *Boyd* used government-owned property for its own commercial advantage and profit was a sufficient basis upon which the Court could uphold the Tennessee tax on the authority of the so-called "Michigan cases." See *United States* v. *City of Detroit*, 355 U.S. 466 (1958); *United States* v. *Township of Muskegon*, 355 U.S. 484 (1958).[6] Thus, to the extent that the Court in *Boyd* regarded the South Carolina use tax in *Livingston* as comparable to the Tennessee use tax (see 378 U.S. at 45 n.6), the fact that duPont received no fee in *Livingston* offered an additional ground for distinguishing that case. While we believe that the South Carolina use

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[5] The sales tax question in *Boyd* was litigated only through the Tennessee Supreme Court. As we discuss (pages 38-40, *infra*), that aspect of the case bears upon the New Mexico taxes at issue here.

[6] The "privilege"-type use tax is valid only to the extent it segregates the contractor's interest in the government-owned property. *United States* v. *State of Colorado*, 627 F.2d 217 (10th Cir. 1980), aff'd, No. 80-714 (Feb. 23, 1981). There, the court below held that a Colorado property tax upon a private contractor engaged to manage a federal atomic facility violated the federal government's constitutional immunity from state taxation, where such tax did not segregate whatever limited interest the contractor had in the use of the government-owned property to perform the contract but was based upon the fair market of the property. The county's failure to limit the tax to the contractor's interest was evidenced by the fact that the tax amounted to almost twice the contractor's fixed management fee. See also *United States* v. *County of Allegheny*, *supra*.

tax in *Livingston* is more properly viewed as a compensating use tax meant to complement a sales tax by levying a tax upon out-of-state purchases (see, *e.g.*, *General Trading Co.* v. *State Tax Commission*, 322 U.S. 335, 336-337 (1944)) and therefore different from the privilege-type use tax in *Boyd*, it has never been disputed that the New Mexico use tax at issue here is a compensating use tax. See *Mescalero Apache Tribe* v. *Jones*, 411 U.S. 145, 158 (1973). Hence, the fact that two of the contractors in this case (Zia and LACI) earned a fee has no relevance.[7] Moreover, given the difference between the use tax involved in *Boyd* and the New Mexico use tax in the instant case, the court of appeals' reliance (Pet. App. 20a n.7) upon this Court's use tax holding in *Boyd* is misplaced.

If any further demonstration of the viability of *Kern-Limerick* as a precedent is required, the Court's recent decision in *United States* v. *County of Fresno*, *supra*, 429 U.S. at 459-460 n.7, should conclusively settle the matter. While the Court in that case found *Kern-Limerick* to be distinguishable, it cited the case as standing only for the proposition that "the State may not impose a tax the legal incidence of which falls on the Federal Government."

It is precisely that proposition upon which we rely in challenging the validity of the state taxes at issue in this case. Here, it is undisputed that the legal incidence of both the New Mexico gross receipts and compensating use tax is on the contractors. Indeed, the court below so held in a prior case involving defense contracts that "specifically provide[d] that the contractors [were] not acting as agents of the United States." *United States* v. *State of New*

[7] The imposition of the New Mexico gross receipts tax on these fees is not in dispute. See page 6 note 3, *supra*.

Mexico, 581 F.2d 803, 806 (10th Cir. 1978). In so ruling, however, the court below acknowledged—citing *Kern-Limerick*—that "[i]f the United States desires to avoid enriching state coffers with federal funds, it can easily do so by changing the terms of its contracts" (*id.* at 808 n.1).[8]

We submit that the terms of the standard federal contract for the management of atomic facilities accomplish exactly that result in accordance with the guidelines established by this Court in *Kern-Limerick* and in *Livingston*, with reference to contracts indistinguishable from the instant arrangements.[9]

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[8] The court drew further support for its conclusion that the defense contractors in *United States* v. *State of New Mexico*, *supra*, were not agents of the United States from the trial court's finding "that at least since 1955, it has been the policy of the Department of Defense not to include in its contracts agency-creating clauses to avoid state and local taxes otherwise payable by its contractors" (581 F.2d at 808 n.1). See also *United States* v. *Forst*, 569 F.2d 811 (4th Cir. 1978).

[9] It is clear that *Kern-Limerick* is the pertinent precedent for determining whether contractors under the standard federal contract for the management of atomic facilities qualify for the constitutional immunity of the federal government from state and local taxation.

The origin of the particular management contract involved in this case derives from the arrangements to develop atomic weapons made during World War II between the federal government (through the Manhattan Engineering District) and various universities and industrial organizations. After the cessation of hostilities, the responsibilities of the Manhattan Engineering District were transferred to the Atomic Energy Commission by the Atomic Energy Act of 1946, ch. 724, 60 Stat. 755 *et seq.* The Atomic Energy Act of 1946 provided that the Atomic Energy Commission would be the sole owner of certain nuclear materials and the facilities to produce nuclear weapons, and directed the Commission to

Just as in *Kern-Limerick*, the standard atomic management contract clearly designates the contractor as a procurement agent of the United States so that

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contract for the operation of these facilities (Section 4(c)(1) and (2)). The Commission continued the practice of contracting with private parties under the Atomic Energy Act of 1954, 42 U.S.C. 2011 *et seq.* Accordingly, there has been a longstanding and unique partnership between the government and private industry arising from the government's monopoly of nuclear materiel production (see 42 U.S.C. 2061(a)) and industry's technical capacity to accomplish that production under government contract.

Congress was not unaware of the possibility that local governments might seek to tax the activities of contractors engaged by the Atomic Energy Commission. Thus, Section 9(b) of the 1946 Act expressly exempted the "property, activities, and income" of the Commission from local taxation. When this was eventually challenged as applied to the Commission's contractors, this Court in *Carson* v. *Roane-Anderson Co.*, 342 U.S. 232 (1952), held that two such contractors were performing "activities" for the Commission, and were exempt from local taxation. Accord, *General Electric Co.* v. *Washington*, 347 U.S. 909 (1954). Shortly after the *Carson* decision, Congress repealed Section 9(b), expressing the view that the Atomic Energy Commission and its contractors should be in the same position as other federal agencies with respect to immunity from state and local taxation. Act of August 13, 1953, ch. 432, 67 Stat. 575. See S. Rep. No. 694, 83d Cong., 1st Sess. (1953), discussed in *Kern-Limerick* v. *Scurlock*, *supra*, 347 U.S. at 117, and in *United States* v. *Boyd*, 378 U.S. 39, 49-50 & n.10 (1964). But as the Court pointed out in *Kern-Limerick*, *supra*, 347 U.S. at 117, "in recommending the legislation the Joint Committee on Atomic Energy, while providing for voluntary contributions, did not propose to subject Government property and purchases to state taxes. The enactment left them free. This recognition of the Constitutional immunity of the Federal Government from state exactions rests, of course, upon unquestioned authority" (footnote omitted).

the federal government was the disclosed purchaser.[10] Since the contractors here are disbursing and procuring agents of the government, the legal incidence of the New Mexico tax is on the government; hence, the tax cannot validly be imposed upon them.

Finally, in rejecting the government's claim of contractor immunity under the standard atomic facility management contract, the court of appeals observed that its "reiterated antipathy to wholesale deprivations of state treasuries without congressional action, requires, at the least, some special arrangement before tax immunity attaches" (Pet. App. 21a). But, as this Court demonstrated by its summary affirmance of the three-judge district court in *Livingston*, the advanced funding procedure employed under the contracts at issue constitutes the very type of "special arrangement" that effectively insulates these federal contractors from state sales and compensating use taxes. A detailed examination of the contracts between Sandia, Zia, and LACI and the Department of Energy, to which we now turn, establishes the tax immunity of the contractors in this case under the foregoing legal principles.

C. The Contractors in This Case Qualify for State Tax Immunity Under the Criteria Established in *Kern-Limerick, Inc.* v. *Scurlock*, 347 U.S. 110 (1954)

1. In *Kern-Limerick*, the Court cited the following facts to support its determination that sales to the contractor acting as a purchasing agent for the

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[10] The standard atomic management contract is therefore significantly different from the defense contracts at issue in *United States* v. *State of New Mexico, supra*. There is accordingly no basis for the court of appeals' characterization of the argument that Sandia, Zia, and LACI are procurement agents of the government as "at odds with the [defense] contracts discussed" in its own prior decision (Pet. App. 19a).

United States were therefore immune from state sales tax. First, title to all materials and supplies purchased vested in the government directly and the contractor never acquired any title to the goods (347 U.S. at 112 n.2, 119-120). Second, the contract required "specific Government approval to the purchasing agent for each request for bid and each purchase" (*id.* at 120; see also *id.* at 112 n.2). Third, the request for bids explicitly stated: "This purchase is made by the Government. The Government shall be obligated to the Vendor for the purchase price, but the Contractor shall handle all payments hereunder on behalf of the Government" (*id.* at 119). Finally, the contract provided that "[t]he Contractor shall act as the purchasing agent of the Government in effecting such procurement and the Government shall be directly liable to the vendors for the purchase price" (347 U.S. at 112 n.2). The Court therefore concluded that "[u]nder these circumstances, it is clear that the Government is the disclosed purchaser and that no liability of the purchasing agent to the seller arises from the transaction" (*id.* at 120-121; footnote omitted).

In sum, the purchasing agency relationship between the government and the contractor rested upon: (1) immediate passage of title from the vendor to the government; (2) governmental approval for purchases; (3) specific notice to the vendor that the purchase in question is being made by the government; and (4) explicit characterization of the contractor as a purchasing agent of the government. An examination of the contracts and other pertinent documents in the present case demonstrates that Zia, Sandia, and LACI all qualified for tax immunity as purchasing agents of the United States under the rule of *Kern-Limerick.*

a. *Title to Goods.* In accordance with each contract, "title to all materials, equipment, supplies, and tangible personal property of every kind and description purchased by the Contractor, for the cost of which the Contractor is entitled to be reimbursed as a direct item of cost under this contract, shall pass directly from the vendor to the Government" (J.A. 20b; see also 13, 231a (Zia); 34, 151 (Sandia);[11] 29 (LACI)). Hence, it cannot be seriously questioned that the direct passage of title from the vendor to the United States was precisely the same as in *Kern-Limerick.*

b. *Government controls.* Moreover, each of the contracts provides an extensive system of government controls over the contractors' activities that serves the same purpose as the required governmental approval for each purchase in *Kern-Limerick.* For example, each contractor is obligated to "prepare and submit annually as of June 30, a voucher, for the total of net expenditures accrued (i.e., net costs incurred) for the period covered by the voucher, and the [Atomic Energy] Commission, after audit and appropriate adjustment[,] will approve such voucher" (J.A. 20 (Zia); 27 (LACI)). See also J.A. 31-32 (Sandia) (written approval of Commission required for advances in excess of $15,000). In addition, the contractors are required to establish and maintain property management systems, bonding and insurance and financial plans with cost limitations, and to appoint key personnel acceptable to the gov-

[11] The passage-of-title clause in the Sandia contract employs somewhat different wording but the legal effect is the same. It provides: "Title to all property of any kind whatsoever acquired by Sandia Corporation shall pass to the Government when it passes from the vendor, except as may be directed by the Commission" (J.A. 34).

ernment (J.A. 21a (Zia); 22, 23-25 (LACI); 37, 46 (Sandia)). Moreover, any disputes under the contracts which were not resolved by the contractor and the vendor were to be resolved by the appropriate DOE contracting official (see J.A. 128-129, 157-158). Thus, while the contractors in this case operated with somewhat greater autonomy on a day-to-day basis than *Kern-Limerick*, they were likewise fully accountable to the government for their purchases and actions. The difference in governmental control between this case and *Kern-Limerick* is one of degree and not of kind. Moreover, this factor is not as significant here, in light of the advanced funding present in this case, but not in *Kern-Limerick* (see pages 32-35, *infra*).

c. *Notice of third parties.* Furthermore, the third-party vendors of goods and services in this case were equally aware that the dealings of Zia, Sandia, and LACI with them were on behalf of the United States. Just as the request for bids in *Kern-Limerick* explicitly advised the third party that "[t]his purchase is made by the Government" (347 U.S. at 119), here, too, the face of the contractors' checks specifically stated that they were drawn against government funds. Thus, Zia's checks bore the legend "A.E.C. ADVANCE FUNDS/PAYROLL ACCOUNT/NOT TO EXCEED $500" (Exh. 19, J.A. 99) or "U.S. ENERGY RESEARCH AND DEVELOPMNT ADMINISTRATION/ADVANCE FUNDS ACCOUNT" (Exh. 21, J.A. 101). Sandia's checks similarly stated: "SANDIA LABORATORIES/ALBUQUERQUE, NEW MEXICO 87115/OPERATED BY SANDIA CORPORATION/for/ENERGY RESEARCH AND DEVELOPMENT ADMINISTRATION/ADVANCE FUNDS ACCOUNT" (Exh. 20, J.A. 100).[12]

[12] The facts that there were earlier Sandia checks (Exh. 18, J.A. 97-98) and a LACI check (Exh. 19, J.A. 99)

d. *Characterization of the contractors as purchasing agents.* That the parties intended that Zia, Sandia, and LACI were to be purchasing agents of the government is demonstrated by the advanced funding arrangement and confirmed by the contract modifications.

(1) *Advance funding.* As we have pointed out (pages 4-5, *supra*), under the advanced funding procedure, the contractor, the United States, and a designated bank open a special bank account pursuant to a three-party contract (J.A. 111-113). The United States owns the balance in the account and all revenues under the contract are government property required to be deposited in the account. However, the contractor is empowered to issue drafts to third parties for expenses incurred under the contract (*id.* at 20, 26, 27, 82-83a, 84-90a). The general authority for the funding of the bank account originates in a letter of credit issued by DOE to the Federal Reserve Bank in favor of the contractor (*id.* at 82-83a, 92-93, 95, 96). When the contractor issues a check to a third party, it also issues a voucher, which it forwards to the Federal Reserve Bank. As a result,

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introduced into evidence that do not state on their face that they were drawn on government funds, does not cast substantial doubt upon our submission that the third party vendors were aware that all three contractors were acting on behalf of the government. Both Sandia and LACI were organized for the sole purpose of serving as government contractors. Neither was involved in any private work (see J.A. 31). Indeed, LACI (a subsidiary of Zia) was exclusively involved in construction work in support of the Los Alamos Scientific Laboratory, a government-owned facility. LACI owned no tangible personal property and procured all of the property it required from Zia (Pet. App. 3a, 14a). Hence, no third party could have been unaware that Sandia and LACI were procurement agents of the government.

the Federal Reserve Bank deposits an equivalent sum to the account of the designated bank of deposit, which in turn credits the special bank account with sufficient funds to cover the draft. See J.A. 81-83a, 91-94.

The foregoing description of the advanced funding procedure convincingly demonstrates that the contractors were procurement agents of the United States. Here, it is beyond question that the contractors did not even have to expend any of their own funds for goods or services but were able to disburse monies that at all times belonged to the government. Surely that power to spend government money "gave to the contractors the status of agents of the Government to enter into contracts or to pledge its credit." *Alabama* v. *King & Boozer*, *supra*, 314 U.S. at 13. As the Fourth Circuit correctly observed in *United States* v. *Forst*, *supra*, 569 F.2d at 811, "the key factor in the case was whether the credit of the United States or the contractor was bound by the purchasing agreements." Since Sandia, Zia, and LACI were empowered to write checks on government-owned funds, their power to bind the United States and pledge its credit cannot seriously be questioned.

Contrary to the court of appeals' conclusion, the advanced funding procedure cannot be dismissed as "simply another means of reimbursement devised by accountants * * *" (Pet. App. 23a). There is a considerable difference between the case where the contractor expends its own funds and must await reimbursement by the government and the case in which the contractor is empowered to draw directly on the funds of the government. While the former case may not be inconsistent with an agency relationship (as *Kern-Limerick* itself demonstrates), it

is at least clear that in such a case the contractor must rely upon the government's ratification of its actions in order to obtain reimbursement for its outlays. Here, the contractors did not even take that risk, for they disbursed government funds to the vendors and to their employees in the first instance. In every sense of the word, the contractors here acted on behalf of the government vis-a-vis the vendors. If the contractor receiving after-the-fact reimbursement in *Kern-Limerick* was deemed to be an agent of the United States so that sales to it were thereby immune from state taxes, the case for immunity here follows a fortiori because the contractors had the additional authority to disburse government funds and pledge the credit of the United States.

Although the court of appeals acknowledged that the advanced funding procedure created "appearances" of agency status for the contractor (Pet. App. 22a), it resisted the conclusion that the contractors were immune from state taxes, relying on the fact that "[a]t most, the contractor may pledge to the limit of its letter of credit" (*id.* at 22a-23a). As the court reasoned, "[s]een in this light, Sandia, Zia and LACI are like numerous businesses which deal under letters of credit from banks and other sureties" (*id.* at 23a).

But the conclusion that the contractors' purchases and disbursements are subject to state gross receipts taxes does not follow from the fact that their letters of credit are limited in amount. The claim of immunity here is only coextensive with the contractors' authority to act on behalf of the government. The fact that their authority, like the authority of many agents, is limited in dollar amounts does not refute the argument that they act as agents of the government when acting within the scope of their authority.

Simply because there is some limit upon an agent's authority does not cast doubt upon the existence of the agency relationship itself.

(2) *Contract Modifications.* Finally, if any doubt remains as to the procurement agent status of the contractors in this case, it is dispelled by the modifications to the contracts made as of July 1, 1977. The typical modification recited in pertinent part as follows (J.A. 49-52): [13]

> WHEREAS, the parties recognize that under this contract and the long-standing relationship and practice of the parties hereunder Sandia Corporation acts and has acted as an agent for and on behalf of ERDA [Energy Research Development Administration—now part of DOE] and the Commission for certain purposes; and
>
> WHEREAS, for the benefit of persons who are not parties and not familiar with the contractual relationships and practices hereunder, the parties desire to have the contract reflect the long-standing agency status and authority of Sandia Corporation for certain purposes; * * *
>
> * * * * *
>
> The following article is added to the contract as Article XX:
>
> *Article XX. Status and Authority of Sandia Corporation as an Agent of ERDA*
>
> Under the provisions of this contract, Sandia Corporation has performed and will continue to perform as a management contractor of ERDA. On the basis of certain provisions of this contract and the long-standing relationship and practice of the parties hereunder, it is recog-

[13] There are comparable modifications of the contracts with Zia (J.A. 54-57) and LACI (*id.* at 58-61).

nized that Sandia Corporation acts as an agent for and on behalf of ERDA for certain purposes. Particular provisions and features of the contractual relationship which establish the agency status of Sandia Corporation and the extent of the status and authority thereby created include, but are not limited to, the following:

1. Only ERDA funds are to be used in the performance of this contract by Sandia Corporation, and no funds of Sandia Corporation or of Western [Electric] are required. The funds of ERDA made available for performance of this contract pursuant to the provisions hereof and pursuant to any special bank accounts established hereunder, including all revenues received by Sandia Corporation in the conduct of operations hereunder, are and shall remain the funds of ERDA until expended and shall not at any time become the funds of Sandia Corporation or Western. Sandia Corporation acts as agent for and on behalf of ERDA in disbursing ERDA funds, by the drawing of checks on special bank accounts or by any other method approved by ERDA, for the payment and satisfaction of all obligations properly incurred by Sandia on behalf of ERDA in accordance with the provisions of this contract.

* * * * *

2. * * * Sandia Corporation in the performance of this contract acts as the agent of ERDA in the purchase, lease, or other acquisition, and in the management, maintenance, protection, safeguarding, sale, and disposition of all property of any kind whatsoever, real or personal, used in the performance of this contract.

* * * * *

> 4. ERDA considers all obligations properly incurred in accordance with the provisions of this contract to be ERDA obligations from their inception. Sandia Corporation acts as agent of ERDA in making appropriate payments to all obligees and is responsible for taking any and all other actions as may be necessary for appropriate and timely discharge of all such ERDA obligations. The purpose of this article is to recognize and express existing relationships. This article shall not be construed to modify any other provisions of the contract nor shall it create rights or obligations not otherwise provided for in the contract.

In holding that Zia, Sandia, and LACI were not tax-immune procurement agents of the United States, the court of appeals rejected the plain meaning of the foregoing contract modifications on the ground that they conclude with the caveat that they "shall not be construed to modify any other provisions of the contract * * * nor shall [they] create rights or obligations not otherwise provided for in the contract" (J.A. 57). As the court stated, "[b]ecause we are convinced that, as a matter of law, the provisions of the contracts before the amendments did not establish agency status, we need not be swayed by amendments which make no changes" (Pet. App. 26a).

But the court of appeals' analysis misses the point of the contract modifications. They were not designed to alter the substantive relationship provided by the contracts but to confirm the "agency status of the Contractor * * * [to] include * * * the following: * * * The Contractor acts as agent for and on behalf of ERDA in disbursing ERDA funds * * * [and] the Contractor is authorized to pledge the

credit of the United States in any and all such [purchasing, leasing, and acquisitions of property] transactions, contracts, and other arrangements" (J.A. 55-56). Indeed, in quoting from the clause that stated that the modifications were not to alter any other provisions of the contract, the court omitted the phrase "including, but not limited to, the article entitled Allowable Costs, Base Fee and Award Fee)" (*id.* at 57). See also *id.* at 61. Cf. *id.* at 52. The omitted phrase shows that in confirming the contractors' status as procurement agents, the parties did not intend to modify any other substantive rights and obligations under the contracts.[14]

2. At all events, the fact "that the agency terminology does not appear uniformly in all the documents relating to the contracts" (Pet. App. 26a) does not effectively distinguish this case from *Kern-*

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[14] Contrary to the court of appeals' further observations (Pet. App. 26a), the facts that the purchase orders refer to the contractors as the "Buyer" (see J.A. 120) and that Sandia's contract requires it to make purchase orders in its own name (see J.A. 36-37) does not support its conclusion that the contractors were not procurement agents. As we have pointed out (see page 31, *supra*), the contractors' checks or their identities fully advised third parties that they were dealing with procurement agents for the government. Moreover, the same purchase order (cited by the court of appeals) that refers to the contractor as the "Buyer" modifies that term with the phrase "in the performance of the prime contract * * *," *i.e.*, pursuant to which it acts as a procurement agent (J.A. 120). Finally, while the Sandia contract requires Sandia to make purchase orders in its own name, it further requires that "Sandia Corporation shall insert in such purchase orders * * * such clauses respecting Government property * * * as the Commission may require * * * [and] shall observe the Commission's requirements respecting acquisition and use of property" (*id.* at 37).

Limerick, as the court of appeals apparently believed. Much the same argument was advanced by the State of Tennessee and rejected by the Tennessee Supreme Court in *United States* v. *Boyd*, 211 Tenn. 139, 363 S.W.2d 193 (1962), aff'd on another issue, 378 U.S. 39 (1964). There, the Tennessee court held that the contractor under the identical standard DOE management contract with advanced funding was immune from state sales taxes. In response to the argument that the contract did not in all respects employ the identical *Kern-Limerick* terminology of "agency," the court stated, in terms that are equally appropriate here (211 Tenn. at 155; 363 S.W.2d at 200):[18]

> The mere placing of terms such as agent or independent contractor in the contract does not make them such in law. The surrounding facts and circumstances determine the relationship.
>
> * * * It appears from the contract and from the actions of the parties that the relationship of agency in so far as the purchase of materials are [sic] concerned when accomplished in ac-

[18] The aspect of *Boyd* upon which we rely is the sales tax portion of the case that was considered by the Tennessee Supreme Court, which the State did not appeal to this Court (see 378 U.S. at 43 n.5). The issue before this Court was the constitutionality of the state use tax as applied to the contractor. This Court affirmed the Tennessee Supreme Court's holding that the State could impose a tax on a government contractor on the use of tangible personal property for private gain in the performance of a contract because the contractor's property had not been "so incorporated into the government structure as to become instrumentalities of the United States and thus enjoy governmental immunity" (*id.* at 48). However, as we have pointed out (pages 23-25, *supra*), the Tennessee use tax involved in *Boyd* was not a compensating use tax of the type involved here. The decision of this Court in *Boyd* therefore has no bearing on this case.

> cordance with the contract bring them within the holding of Kern-Limerick and under that case the A.E.C. is the purchaser. Therefore, the Sales Tax would be a direct tax upon the Government and is invalid under the doctrine of implied immunity, and we so hold.

To the same effect is *United States* v. *Nevada Tax Commission*, 291 F. Supp. 530 (D. Nev. 1968), aff'd, 439 F.2d 435 (9th Cir. 1971), a case that the court of appeals here conspicuously ignored, and which likewise cannot be squared with the decision below. There, as here, the state sought to impose its sales and compensating use tax upon a government contractor's purchase and use of tangible personal property under the identical standard DOE contract. In accordance with the advanced funding procedure, the contractor purchased the property with government-owned funds, and title to the property vested immediately in the government. Relying on *Kern-Limerick*, the district court upheld the contractor's claim that the sales were immune from a comparable Nevada sales and compensating use tax modeled after a California statute. As the court there concluded, "all sales by retailers to [the contractor] under this contract, the purchase price being paid by the Government and title passing immediately to the Government, are sales to the United States immune from the Nevada Sales Tax" (291 F. Supp. at 533). The Ninth Circuit affirmed "[f]or the reasons stated in the reported decision of the district court" (439 F.2d at 441).[16]

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[16] See also *United States* v. *Bureau of Revenue*, 87 N.M. 164, 166-170, 531 P.2d 212, 215-218 (Hernandez, J., concurring) (1975). There, the concurring opinion concluded

In sum, we submit that, taken as a whole, the contracts and their implementation, under the advanced funding procedure employed for the management of the government's atomic facilities, demonstrate the existence of an agency relationship for procurement purposes between Zia, Sandia, and LACI, and the United States. The 1977 contracts modifications simply confirm what had always been the case.[17] Although the court of appeals stated that

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that the contractors were immune from the gross receipts tax because they did not "receive" the advanced funds within the meaning of the statute (87 N.M. at 167). As for the compensating use tax, the concurring judge determined, on the authority of *United States* v. *Nevada Tax Commission*, *supra*, that the tax was not applicable because the purchased property at all times belonged to the government and was therefore exempt under the statute (87 N.M. at 170).

[17] At the outset, there was no need for the parties to confirm the agency relationship because the State had previously recognized that the contractors were procurement agents "for a period of about twenty years before these modifications were made" (Pet. App. 6a). See also J.A. 223-230. During this period, the State did not seek to impose taxes either on the advanced funds or on the sales to the government through the contractors.

Nor is there any basis for the State's argument in the courts below that without congressional authorization, the government had no authority to modify the contracts for the purpose of achieving tax immunity. As the district court succinctly stated, "This argument is disposed of by the conclusion that the Government and the contractors herein maintained an agency relationship for procurement purposes during the years of operation prior to the contract modifications, and have continued to do so to the present. They were not taxable before the modifications, because such modifications merely made the relationship more express, but did not change the agency relationship which had been in operation for three decades, and which had been recognized as such by the Bureau [of Revenue]" (Pet. App. 6a).

it was "highly skeptical of the sporadic addition of 'magic words' to a contract in an attempt to avoid state taxation" (Pet. App. 26a), this Court in *Kern-Limerick* specified, to the contrary, that "the form of contracts, when governmental immunity is not waived by Congress, may determine the effect of state taxation on federal agencies, for decisions consistently prohibit taxes levied on the property or purchases of the Government itself" (347 U.S. at 122-123; footnotes omitted). The explicit terms of these contracts establishes the governmental immunity of the contractors' purchases for the United States from state sales and use taxes.

CONCLUSION

The judgment of the court of appeals should be reversed.

Respectfully submitted.

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SEPTEMBER 1981

APPENDIX

N.M. Stat. Ann. 1953 (Supp. 1975):

§ 72-16A-3. *Definitions.*—As used in the Gross Receipts and Compensating Tax Act [72-16A-1 to 72-16A-19]:

* * * * *

B. "buying" or "selling" means any transfer of property for consideration or any performance of service for consideration;

* * * * *

E. "engaging in business" means carrying on or causing to be carried on any activity with the purpose of direct or indirect benefit;

F. "gross receipts" means the total amount of money or the value of other consideration, received from selling property in New Mexico, from leasing property employed in New Mexico or from performing services in New Mexico, and includes any receipts from sales of tangible personal property handled on consignment but excludes cash discounts allowed and taken, New Mexico gross receipts tax payable on transactions for the reporting period and taxes imposed pursuant to the provisions of the County Sales Tax Act [13-2-30 to 13-2-35], the County Gross Receipts Tax Act [15-55-1 to 15-55-15] or the Municipal Gross Receipts Tax Act [14-61-1 to 14-61-8] which are payable on transactions for the reporting period and any type of time-price differential.

In an exchange in which the money or other consideration received does not rep-

resent the value of the property or service exchanged, "gross receipts" means the reasonable value of the property or service exchanged.

* * * * *

"Gross receipts," for the purposes of the business of buying, selling or promoting the purchase, sale or leasing, as factor, agent or broker, on a commission or fee basis, of any property, service, stock, bond or security, includes only the total commissions or fees derived from the business;

* * * * *

L. "use" or "using" includes use, consumption or storage other than storage for subsequent sale in the ordinary course of business or for use solely outside this state.

§ 72-16A-4. *Imposition and rate of tax— Denomination as "gross receipts tax."*—A. For the privilege of engaging in business, an excise tax equal to four per cent [4%] of gross receipts is imposed on any person engaging in business in New Mexico.

B. The tax imposed by this section shall be referred to as the "gross receipts tax."

§ 72.16A-7. *Imposition and rate of tax—Denomination as "compensating tax."*—A. For the privilege of using property in New Mexico, there is imposed on the person using property an excise tax equal to four per cent [4%] of the value, at the time of acquisition or of introduction into the state, whichever is later, or of conversion to use by the manufacturer of property that was:

(1) manufactured by the person using the property in the state;

(2) acquired outside this state as the result of a transaction that would have been subject to the gross receipts tax had it occurred within this state; or

(3) acquired as the result of a transaction which was not initially subject to the compensating tax imposed by subsection A(2) of this section of the gross receipts tax but which transaction, because of the buyer's subsequent use of the property, should have been subject to the compensating tax imposed by subsection A(2) of this section or the gross receipts tax.

B. For the privilege of using services rendered in New Mexico, there is imposed on the person using such services an excise tax equal to four per cent [4%] of the value of the services at the time they were rendered. The services, to be taxable under this subsection, must have been rendered as the result of a transaction which was not initially subject to the gross receipts tax but which transaction, because of the buyer's subsequent use of the services, should have been subject to the gross receipts tax.

C. The tax imposed by this section shall be referred to as the "compensating tax."

* * * * *

§ 72-16A-12. *Exemptions.*—Exempted from the gross receipts or compensating tax are those receipts or uses exempted in sections 72-16A-12.1 through 72-16A-12.30 NMSA 1953.

§ 72-16A-12.1. *Exemption—Gross receipts tax —Governmental agencies.*—Exempted from the

gross receipts tax are the receipts of the United States or any agency or instrumentality thereof or the state of New Mexico or any political subdivision thereof.

* * * * *

§ 72-16A-12.2. *Exemption—Compensating tax —Governmental agencies—Indians.*—Exempted from the compensating tax is the use of property by the United States or any agency or instrumentality thereof or the state of New Mexico or any political subdivision thereof.

* * * * *

§ 72-16A-14. *Deductions.*—In computing the gross receipts tax due, only those receipts specified in sections 72-16A-14.1 through 72-16A-14.32 NMSA 1953 may be deducted. Receipts, whether specified once or several times in sections 72-16A-14.1 through 72-16A-14.32 NMSA 1953, may be deducted only once from gross receipts.

* * * * *

§ 72.16A-14.9. *Deduction—Gross receipts tax—Sales to governmental agencies.*—Receipts from selling tangible personal property, other than nonfissionable metalliferous mineral ore, to the United States or any agency or instrumentality thereof or the state of New Mexico or any political subdivision thereof may be deducted from gross receipts. Receipts from selling tangible personal property, other than nonfissionable metalliferous mineral ore, to the governing body of any Indian tribe or Indian pueblo for use on Indian reservations or pueblo grants, may be deducted from gross receipts.

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